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Economic Liberalization and Corruption in the Developmental State: A Case Study of Indonesia in the 1990s

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This article evaluates the claim that economic liberalization reduces corruption in the challenging context of an authoritarian developmental state attempting to open its trade and capital markets while reducing state intervention in the economy. After reviewing the theoretical and empirical evidence behind the assertion that economic liberalization reduces corruption, the claim is considered against the backdrop of Indonesia in the 1990s, a case with high values in both the key variables involved: economic liberalization and corruption. Using newly-available measures of corruption to analyze the Indonesian case, the article points out weaknesses in the "liberalization as remedy" hypothesis and suggests conclusions that may apply to other developmental states. Specifically, it is argued that economic liberalization in the context of an authoritarian developmental state with a large domestic market is unlikely to reduce corruption and quite possibly may contribute to its worsening. The experience of Indonesia in the 1990s may thus hold lessons for other developmental states, especially China, seeking to control corruption while liberalizing large economies under authoritarian rule.

I. Introduction

A common claim that emerges from the literature on corruption and economic development is that economic liberalization—understood here as increasing international trade and capital flow openness while reducing state intervention and regulation in the domestic economy—reduces corruption.[1] Cited by economists and policy-makers alike, this hypothesis has been widely accepted by international financial institutions, including the International Monetary Fund (IMF), which incorporated liberalization measures targeting corruption in its stabilization packages during the Asian financial crisis of 1997–1998. It was this crisis that brought to light pervasive levels of corruption in many of Asia's developmental states, whose explosive economic growth had previously been attributed largely to good governance anchored in technocratic bureaucracies insulated from societal pressures, strong and able political leadership, and the right mix of industrial policy and trade openness.[2] *Yet, despite the apparent*

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1 For a theoretical treatment of the claim that economic liberalization reduces corruption, see Tanzi, 1994. For empirical studies supporting this view, see Ades and Di Tella, 1999; Dreher and Siemers, 2009; Dutt, 2009; Weder, 1999; World Bank, 1997.

2 In this paper, "developmental state" refers to a government that gives precedent to industrial policy concerned with the promotion of a domestic industrial structure that enhances the nation's economic development and international competitiveness. In accordance with Amsden's classifications, this state generally performs four functions: "development banking; local-content management; 'selective seclusion' (opening some markets to foreign transactions and keeping others closed); and national firm formation." Amsden, 2000, p. 125. For other treatments of this model, see Johnson, 1982; Woo-Cummings, ed., 1999.

consensus that, all things being equal, economic liberalization reduces corruption, how strong is the case for economic liberalization as a remedy for corruption in developmental states?

This paper reviews the theoretical and empirical evidence behind the "liberalization as remedy" hypothesis and then reconsiders its claims against the backdrop of the case of Indonesia in the 1990s. Often characterized as a developmental state, Indonesia is an attractive laboratory for considering this hypothesis because its economy has high values in both the key variables involved: economic liberalization and corruption. Using newly-available measures of corruption to analyze the Indonesian case, the paper points out weaknesses in the "liberalization as remedy" hypothesis and suggests conclusions that may apply to other developmental states. Specifically, it is argued that economic liberalization in the context of an authoritarian developmental state with a large domestic market is unlikely to reduce corruption and quite possibly may contribute to its worsening. In this sense, just as some studies have found corruption can be growth-enhancing in certain developmental contexts, this paper argues that economic liberalization can actually breed corruption (or fail to reduce it) in large authoritarian developmental states that roll back interventionist policies.[3] The experience of Indonesia in the 1990s may thus hold lessons for other developmental states, especially China, seeking to control corruption while liberalizing large economies under authoritarian rule.

Before moving forward, a key definition needs to be specified. In this paper, the term "corruption" refers to both public sector venality, understood as the violation of recognized ethical and/or legal norms in the use of public office (often but not always for organizational and/or individual gain) and to violations of recognized ethical and/or legal norms in the use of entrusted power in the private sector (also often but not always for organizational or individual gain, such as embezzlement, fraud, violating capital adequacy requirements, insider trading, etc.).[4] This relatively inclusive definition has been chosen for four reasons. First, it incorporates both the misuse of public office and the often neglected forms of private sector corruption, which can affect and be affected by changes in economic institutions just as much a public malfeasance. Although political scientists and economists have long deemphasized the private sector in their accounts of corruption, there is no valid theoretical justification for ignoring private sector corruption, especially when one considers that vast criminal and ethical breaches by globalized financial institutions nearly collapsed the world economy as recently as 2008. Second, the line between the public and private sector can sometimes be blurry in certain institutional arrangements and the public-private distinction differs from country to country, thereby allowing one to change the meaning of "government corruption" simply by crossing national borders.[5]

A third reason for adopting such an inclusive definition is that many forms of corruption are hybrid

[3] For arguments that corruption can be growth-enhancing, see Kang, 2002; Rock and Bonnett, 2004.

[4] This definition is adapted from Hodgson and Jiang, 2007.

[5] For an early and influential example, see Nye's definition: "Corruption is behavior which deviates from the formal duties of a public role because of private-regarding (personal, close family, private clique) pecuniary or status gains; or violates rules against the exercise of certain types of private-regarding influence." See Nye, 1967, p. 419; Hodgson and Jiang, 2007, pp. 1044–1049.

in nature, requiring both public and private sector participants, and some of these are "bottom-up" or instances of the "rent-seeking of powerful [private sector] groups that overwhelm the state's ability to contain and channel their demands."[6] For example, firms may make election campaign donations to influence politicians to defund or under-staff regulatory agencies in order to allow the firms to commit systematic fraud without serious fear of state monitoring. Here, private sector actors are both the initiators and the major beneficiaries of corruption that involves in part the misuse of public office. Fourth, and important for the Indonesian case study, the conception of corruption adopted here is consistent with the legal definition of corruption in Indonesia's criminal code.[7]

The paper proceeds as follows. The next section reviews the theoretical basis behind the claim that economic liberalization reduces corruption and then surveys quantitative empirical studies that address the relationship between these two variables. The mixed results found in these studies are argued to justify a resort to qualitative methods in the form of a case study to reconsider the theoretical argument. The third section examines patterns of corruption in Indonesia in the 1990s, a period in which high levels of corruption are found in a country that had implemented significant economic liberalization over the previous decade. The concluding section summarizes the findings from the Indonesian case and considers them in the context of research on liberalization and corruption in other country cases.

II. Economic Liberalization and Corruption: Clear Theory, Murky Empirics

The model of corruption represented in the "liberalization as remedy" hypothesis emerges from principal-agent theory in the economics literature.[8] The model comprises three levels: the principal (head of government), the agent (bureaucrat, administrative official), and the client (private sector firm/actor). Focusing on the agent-to-client relationship, "liberalization as remedy" advocates posit that the key to controlling corruption lies in reducing both the potential and the incentive for the agent to use the powers of his or her administrative position to extort illegal payments or privileges from the client. This reasoning leads to two general sets of policy prescriptions. First, the theory suggests that corruption can be reduced by changing the internal incentive structure of the agent. This may be accomplished in a variety of ways, including increasing the penalties for corrupt behavior, strengthening the monitoring capabilities of the principal, and increasing the legal compensation of the agent.[9]

The second (and primary) set of policy prescriptions calls for economic liberalization on two grounds. First, economic liberalization, in the form of the reduction or elimination of trade and capital controls, the deregulation of private industry, and the privatization of state-owned enterprises, reduces

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6 Kang, 2002, p. 182. In economics, rents are payments to or for a factor of production in excess of what the factor's owner could receive from alternative uses. For a discussion of this term in the context of corruption, see Kang, 2002, p. 180.

7 For the definition of "criminally corrupt" in Indonesian law, see Robertson-Snape, 1999, p. 598.

8 For a discussion of the roots of this view, see Klitgaard, 1988, pp. 69–97.

9 Rijckeghem and Weder, 1997; Montinola & Jackman, 2002.

the agent's authority vis-à-vis the client and thus his or her capabilities to extract client resources.[10] Second, by promoting competition in the private sector through increased trade openness and capital market deregulation, economic liberalization programs are said to reduce the large economic rents that both agents and clients can amass as a result of the competition-limiting industrial policies of developmental states.[11] By reducing the availability of "extortable" client rents, liberalization initiatives are seen to lower the incentive for agents to seek bribes in the first place. In this way, economic liberalization is proposed as the key policy tool against corruption in developmental states.

Empirical investigations of the "liberalization as remedy" hypothesis generally take the form of quantitative, cross-country studies. These studies attempt to establish correlations between indicators of corruption and measures of factors theorized to affect the amount and/or frequency of corruption. The latter include economic factors, such as the level of compensation in the public sector, the level of income per capita, the extent of state involvement in the economy, the degree to which rents are available, and the degree of trade protection and capital account restrictions (or overall integration into the world economy); institutional factors, such as the strength of domestic democratic institutions, the amount of time elapsed since democratization, and the presence or absence of certain historical experiences, such as a past as a British colony; and cultural factors, such as measures of social capital and the share of the population with Protestant religious affiliation.[12]

Indicators of corruption used in these studies generally follow one or more of three methodological approaches.[13] The first involves subjective measures drawn from opinion surveys of business managers or populations in the target countries (e.g. corruption indices published by Business International Corporation), assessments provided by the country analysts of international market research firms or other experts (e.g. corruption measure in Political Risk Services Group's *International Country Risk Guide*), or composite indices generated by non-profit or international organizations (e.g. the Transparency International Corruption Perceptions Index (CPI), the World Bank Control of Corruption (CC), etc.). A second, more recently-developed approach focuses on objective data, such as Golden and Picci's use of the difference between measures of the value of public infrastructure and cumulative government spending on public capital stocks to assess the scale of corruption in Italy.[14] Finally, subjective measures are sometimes augmented by objective data, such as measures of anti-corruption prosecutions, to form hybrid measures (e.g. Institute of Management Development's *World Competitiveness*

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[10] Tanzi lists some of the industrial policy instruments that make corruption possible, including regulations (issuance of licenses, zoning, and permits), fines for alleged violations of legal norms, control over procurement and public investments, tax incentive programs, subsidies, and subsidized credit programs, among others. See Tanzi, 1994, p. 11.

[11] Please note that "bribery" is defined in different ways in the literature on corruption. In particular, some make a distinction between "active bribery" in which the client offers money or other undue advantage to the agent in return for the favorable use of his or her public powers and "passive bribery" in which the agent extorts money or other undue advantage from the client in return for the favorable use of his or her public powers. See Malito, 2014, pp. 5–9.

[12] For examples, see Rijckeghem and Weder, 1997; Ades and Di Tella, 1999; Dutt, 2009; Dreher and Siemers, 2009; Lambsdorff, 1999; and Sandholtz and Koeztle, 2000.

[13] This categorization is taken from Malito, 2014, pp. 4–5.

[14] Golden and Picci, 2005.

Yearbook).

It should be noted that all of these approaches have been subject to criticism on a number of methodological grounds. First, many of the cross-country indices of corruption were introduced in the mid-to-late 1990s and thus cannot be used to examine corruption levels at earlier times. Worse yet, the two most well-known such indices, CPI and CC, use a rank-order structure, calculate annual scores using different data sources in different years, and add new countries over time so that it is inappropriate to use rank (or even raw score in CPI) as a measure of change in corruption over time at the country level.[15] In fact, one can only say that these indices measure the relative state of corruption between the countries included in any given year using a given set of data (which may by different in the next iteration).[16] Second, many scholars point to the fundamental weaknesses of subjective data. Whether asking for the opinions of experts, business executives or the general population, surveys assess perceptions of corruption, rather than corruption itself, and human perception is subject to well-known cognitive biases, such as the bandwagon and halo effects, that likely aggravate the already existing mismatch between perceptions and reality.[17] In addition, it has been noted that experiential bias may taint these indices because they rely on surveys of business elites and thus reflect only the views of a small number of multinational firm executives that likely lack exposure to many forms of local private sector and even public sector corruption in the countries they evaluate.[18] Finally, objective indicators of corruption have been criticized because they are inevitably imprecise due to the clandestine nature of the act and "as yet have limited country coverage, and almost no time dimension."[19] Further, detailed efforts such as audits of specific projects may reveal actual corruption but are unlikely to provide information at the country level or be suitable for cross-country comparison or even monitoring over time.[20]

In addition to this lack of consensus over appropriate measures for corruption, the results of quantitative empirical studies on its relationship with economic liberalization have also proven mixed. For example, although Lapalombara asserts a "rough positive correlation" between state involvement in the economy (as measured by government expenditure as a percentage of gross domestic product (GDP)) and measures of corruption, Weder, using a different data set, finds no significant correlation between the two.[21] Scholars looking at the proposed relationship between corruption and the level of economic

15 It should also be noted that the composite indices can be criticized for using surveys that either investigate different aspects of corruption or leave the definition of corruption up to the respondent to determine and thus incorporate measures that may not correspond with the definition of the term held by the aggregating organization.

16 Malito, 2014, pp. 14–15: Thompson and Shah, 2005, pp. 18–21.

17 Malito, 2014, pp. 13–14. As explained by Malito, the bandwagon effect occurs when more and more surveyed individuals respond based on their views of what the common perception is rather than on the basis of their own independent assessment, while the halo effect refers in this case to the tendency to automatically associate corruption with low level levels of economic development, thus leading to inflation in the corruption scores of poorer countries.

18 Rohwer, 2009, p. 50.

19 Kaufmann, et al., 2007.

20 Ibid.

21 Lapalombara, 1994, p. 338; Weder, 1999, p. 110. Montinola and Jackman (2002, p. 147) also find that "government size does not systematically affect corruption."

rents enjoyed by domestic firms have also arrived at conflicting conclusions. Ades and Di Tella, using trade openness (the ratio of imports to GDP) as an indicator of domestic rents, find a significant negative correlation with two different measures of corruption, while Lambsdorff, noting contradictory evidence, cites doubts about the validity of Ades and Di Tella's choice of variables.[22]

Treisman finds a relationship between trade openness and reduced corruption but notes the effect is so "depressingly small" that "the size of reorientation of trade required to make a difference is prohibitive" for all except small, highly-closed economies.[23] Using different measures of trade openness (indicators of protectionist trade policies) but similar measures of corruption, Dutt disputes Treisman's conclusion, finding instead that protectionist trade policies, particularly government licensing, are strongly significant causes of increased corruption (presumably among agents in the trade bureaucracies).[24] Gerring and Thacker, while also showing that open trade and investment policies and low regulatory burdens correlate with low levels of political corruption, find no such relationship between corruption and the size of the state and conclude that "interventionist states, as measured by public spending, are not necessarily more corrupt."[25] Numerous such examples of conflicting evidence among quantitative studies of corruption have caused one enthusiastic advocate of this approach to admit that "to derive clear arguments with respect to causality is rather difficult."[26]

Over the last decade and a half, a number of scholars have begun to come to grips with the so-called East Asian paradox or "the achievement [by a number of East Asian countries] of very high growth rates in real income per capita over relatively long periods of time in the face of quite high levels of corruption."[27] This research seeks to understand how certain highly-interventionist developmental states succeeded in fostering increases in economic growth and investment that generated widely-spread benefits while allowing large amounts of corruption in both the public and private sectors. Considering South Korea, Kang posits that the combination of a coherent state (one able to maintain both autonomy from societal pressures and internal control over the bureaucracy) and a concentrated business sector (populated by a small number of large, diversified business groups known as *chaebol*) created a "mutual hostages" situation in which neither the state nor the powerful business groups were strong enough to overwhelm the demands of the other, resulting in a long-term public-private sector collusion that limited the level of rents and spread their benefits equitably among the players. Arguing that this model explains how corruption failed to derail development under the Park Chung-hee government, Kang locates this political economy of corruption midway between the worst-case outcomes that occur when the state dominates the business sector (top-down "predatory state") or vice-versa (bottom-up unconstrained "rent-seeking") and the optimal case in which there are numerous business groups and power

22 Ades and Di Tella, 1997, pp. 1029–1030; Ades and Di Tella, 1999, pp. 985–991; Lambsdorff, 1999, p. 5.

23 Treisman, 2000, p. 439.

24 Dutt, 2009, p. 168.

25 Gerring and Thacker, 2005, p. 233.

26 Lambsdorff, 1999, p. 14.

27 Rock & Bonnett, 2004, p. 1000; Kang, 2002; Rock, 2003.

is not concentrated within the state ("laissez-faire" with residual but low levels of corruption).[28]

Applying Kang's model to Indonesia under Suharto, Rock finds some similarities. Although emphasizing other factors, such as the ruling regime's genuine commitment to development and deft hand at coalition-building, he agrees that "the opportunity for mutual gain [among small numbers of government officials and *cukong* business entrepreneurs] reinforced Suharto's basic commitment to development as the adoption of pro-growth development polices enabled him to collect more dividends."[29] In a subsequent quantitative analysis, Rock and Bonnett find that although corruption hampers growth and investment in most developing societies, especially small ones, it actually increases growth in large East Asian developmental states with "stable and strong governments with close and corrupt ties to big business."[30] How can this be? First, they theorize that large countries with big labor forces and domestic markets can continue import substitution policies for longer than smaller countries and are also less likely to be disciplined for corruption by foreign investors eager to gain access to domestic labor and product markets.[31] They find, for instance, that the small size of Asian tigers such as Hong Kong and Singapore, among other factors, likely encouraged them to fight corruption as they opened their economies to Western markets and investment. Second, although they acknowledge that Kang's "mutual hostages" model may explain Japan and South Korea, Rock and Bonnett suggest that other high-corruption, high-growth/investment success stories stem from the presence of strong, highly centralized states that both are committed to growth and development as means to maximize gains from corruption and retain monopoly control over domestic corruption networks, thus keeping corruption growth-oriented and constrained within limits set by the state.

What happens when the strong state at the center of both Kang's and Rock and Bonnett's models of the successful but spotted Asian tiger is liberalized politically, through democratization, or economically, through deregulation and state retreat from interventionist policies, or both? Kang argues that democratization increased the role of money politics and corruption in Korea by fragmenting the state and thus shifting the power balance between the state and business decisively in favor of the latter.[32] With the state no longer able to counter the demands of the concentrated business sector, corruption increased in democratic Korea as private sector rent-seeking went unchecked. This echoes the experiences of many Latin American countries, which saw similar increases in corruption, especially when transitions from authoritarian to democratic governments occurred simultaneously with the dismantling of the developmental state and shift to market-oriented, neoliberal economic policies.[33] The next section considers the case of Indonesia in the 1990s, a period that followed extensive economic liberalization that reduced the interventionist capacities of the developmental state but without significant

[28] In this last instance, competition within and across the public and private sector keeps corruption at low levels. Kang, 2002, pp. 182–184.

[29] Rock, 2003, pp. 30–32.

[30] Rock and Bonnett, 2004, p. 1000.

[31] Large countries are defined as those with populations in excess of 20 million. Ibid., p. 1011.

[32] Kang, 2002, pp. 193–200.

[33] Weyland, 1998.

political liberalization to complicate the picture.

III. Case in Point: Indonesia in the 1990s

The failure of cross-country quantitative research to produce consistent conclusions regarding the "liberalization as remedy" hypothesis points to the potential usefulness of a qualitative approach. In advocating a mixed methods approach, Lieberman argues that case studies are the logical next step when exploring a phenomenon for which quantitative analysis has failed to produce satisfactory results.[34] At this stage, to facilitate the building of a new theoretical model, he recommends the selection of "off-the-line" cases that are "not well predicted by the best-fitting statistical model" and for which there are high quantities of the dependent variable present.[35] This section provides a case study of the relationship between economic liberalization and corruption in Indonesia in the 1990s in order to reconsider the key claims of the "liberalization as remedy" hypothesis. Fitting Lieberman's criteria above, the case of Indonesia during this period was selected because it has high values on both the explanatory (economic liberalization) and dependent (corruption) variables, a condition thought likely to provide insight into the relevant causal relationships.[36]

Although well-documented evidence of corruption is elusive in most cases, virtually all indicators, whether systematic or anecdotal, point to massive levels of corruption in the Indonesian economy during this period. As of the end of the 1990s, Indonesia was consistently ranked near the top on all major corruption indices, and was rated the most corrupt country in three different rankings between 1995 and 2000.[37] In addition, anecdotal evidence places rampant corruption as a major factor in the duration and severity of the Asian financial crisis in Indonesia.[38] On the other hand, however, Indonesia's economic liberalization reforms, which began in the early 1980s, had been praised by international financial institutions as wide-ranging and significant.[39] A 1992 World Bank report even cited Indonesia's deregulation efforts as "one of the Bank's greatest success stories overall in the 1980s."[40] If economic liberalization reduces corruption, what explains this apparent discrepancy? The analysis begins with an assessment of Indonesia's deregulation efforts.

Following the collapse of world oil prices and the stagnation of Indonesia's oil-dependent economy in the early 1980s, a group of Western-trained "technocrats" within President Suharto's New Order regime initiated a decade-long series of economic liberalization reforms designed to promote economic

[34] Lieberman, 2005, p. 443.

[35] Ibid., p. 445.

[36] For another account of this technique, see Van Evera, 1997. p. 70.

[37] For corruption rankings, see Transparency International; IMD, 2000, p. 417; Robertson-Snape, 1999, p. 589. Indonesia was rated the most corrupt country among those surveyed in the Corruption Perceptions Index in 1995 and the World Competitiveness Report survey in 2000 as well as the most corrupt among Asian countries in the Political and Economic Risk Consultancy poll in 1997.

[38] Pincus and Ramli, 1998, p. 724; Cole and Slade, 1998, pp. 61–66; Brown, 2006.

[39] See World Bank and IMF comments praising Indonesian deregulation efforts in MacIntyre, 1993, p. 125; Pincus and Ramli, 1998, pp. 723–724.

[40] World Bank, 1992b, p. 41.

growth by attracting foreign direct investment and fostering competition and expansion in the (non-oil) manufacturing sector.[41] These liberalization reforms proceeded along three major avenues: the deregulation of the trade regime, liberalization in the finance sector, and privatization of some state-owned enterprises. Trade reforms included extensive tariff reductions and a major overhaul of the customs system, which transferred most customs duties from an allegedly corrupt national customs bureaucracy to a private Swiss firm.[42] In addition, reformers successfully abolished a large number of import monopolies, including politically sensitive steel and plastics monopolies, which both involved firms with familial ties to President Suharto. These deregulation efforts, praised by the World Bank, were widely credited with spurring growth in the private sector, increasing trade, and contributing to the diversification of Indonesia's industrial base.[43]

Liberalization of the financial sector was more extensive. Reforms included the elimination of interest rate restrictions and credit ceilings on banks, the allowance of free entry for new domestic and foreign banks, and the relaxation of foreign ownership restrictions. These measures ignited an explosive expansion in the banking sector. Between 1982 and 1990, banking assets as a share of GDP doubled from 33% to 66%, while private banks' share of total outstanding bank credit tripled from 14% to 42%. Between 1988 and 1990, over 55 new banks were founded, and the number of total bank branches nearly doubled. In 1992, a World Bank report judged these reforms to have given Indonesia "one of the most deregulated and market-based financial systems in the developing world."[44]

The privatization of state-run sectors was the third pillar of the 1980s liberalization effort. Although only five state-owned enterprises were publicly listed by 1997, these reforms created significant opportunities for private sector actors in several key industries, including telecommunications, power generation, banking, and infrastructure projects. Not surprisingly, international financial organizations also heaped praise on this aspect of Indonesia's economic liberalization program.[45]

The extent to which the Indonesian economy was successfully liberalized in the 1980s and early 1990s, while not to be exaggerated, should also not be understated. One measure of economic liberalization that has been directly tied to corruption reduction is the ratio of total imports to GDP.[46] Figure

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41 Soesastro, 1989, p. 854–855; Brown, 2006. Two major sources of pressure for liberalization during the 1980s were foreign business investors from Japan and other East Asian countries, who saw Indonesia as a less attractive investment opportunity than other developing countries in the region due to its relatively closed trade and capital markets, and the World Bank, which repeatedly criticized Indonesia's high tariffs and growing number of import monopolies. With the fall in oil export revenues causing problems for Indonesia's balance of payments and the country's dependence on foreign aid on the rise, technocrats were hard-pressed to take steps to attract foreign investment in the non-oil industrial sector and to appear to follow the advice of the World Bank. See Rosser, 2002, pp. 128–130.

42 Robertson-Snape, 1999, p. 595.

43 The oil sector's share of merchandising exports fell from 81.9% in 1981–1982 to 44.9% in 1990–1991, while non-oil exports increased from $5 billion in 1983 to over $34 billion in 1995. Evidence of diversification in the industrial base includes a 44% increase in the manufacturing sector's share of GDP between 1983 and 1996. IMD rated Indonesia 13 out of 47 countries in terms of trade openness in 1998. Prawiro, 1998, pp. 298–301; Bresnan, 1993, pp. 260–266; IMD, 2000, p. 395.

44 World Bank, 1992a, p. 10. For a more complete summary of this period of bank sector growth, see Bresnan, 1993, pp. 264–266.

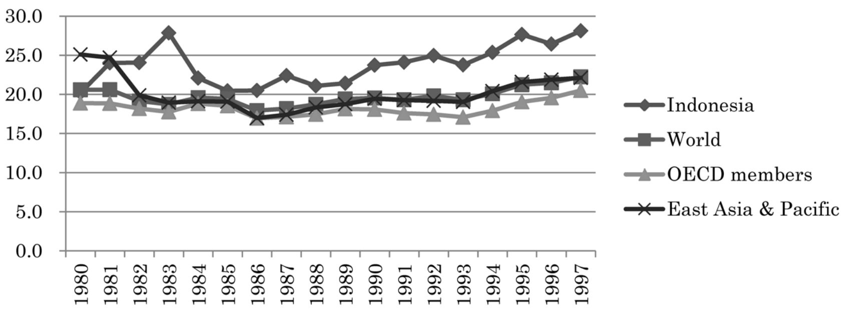
45 Bresnan, 1993, p. 314.

46 For a similar treatment of this variable, see Treisman, 2000, p. 413.

1 below shows changes in the ratio of imports of goods and services to GDP for Indonesia and three major points of comparison from the period just prior to the launch of the liberalization effort to the last full calendar year of the Suharto regime in 1997.[47] After a spike in the early 1980s, when falling oil prices and a global recession intensified the pressure for liberalizing reforms, Indonesia gradually increased its exposure to foreign competition in its domestic markets.[48] In addition, it did so to an extent that exceeded the global and regional averages as well as that of the members of the Organization for Economic Co-operation and Development (OECD), the world's wealthiest countries. In addition, this improvement occurred on a measure that Ades and Di Tella argue captures the level of rents available in an economy for agents to extort from clients.[49] In this understanding, increases in openness to foreign competition should reduce corruption.

Although the above account demonstrates on both the macroeconomic/microeconomic policy levels and the macroeconomic outcome level that Indonesia did in fact implement a significant degree of economic liberalization in the last decade and a half of the Suharto regime, it is important to consider Indonesia's performance vis-à-vis its most-readily comparable competitors, the other large East Asian developmental states. For the comparison, the paper adopts Rock and Bonnett's categorization of Japan and the "large East Asian newly-industrializing countries (NICs)," which include, in addition to Indonesia, China, South Korea, and Thailand.[50] Figure 2 shows how Indonesia fared against these competitors in terms of total imports to GDP ratio from 1980 to 1997. In the exalted company of its

Figure 1 Imports of Goods and Services as a Percentage of GDP, 1980–1997



Source: World Bank (http://data.worldbank.org/indicator (downloaded February 4, 2015))

[47] According to the World Bank, this measure represents "the value of all goods and other market services received from the rest of the world," including "merchandise, freight, insurance, transport, travel, royalties, license fees, and other services, such as communication, construction, financial, information, business, personal, and government services" but excluding "compensation of employees and investment income (formerly called factor services) and transfer payments." See the World Bank website at: http://data.worldbank.org/indicator (downloaded February 4, 2015).

[48] In the period 1983–1997, Indonesia increased the annual average of its total imports as a percentage of GDP by nearly 5% in comparison with the previous fifteen-year period (1968–1982).

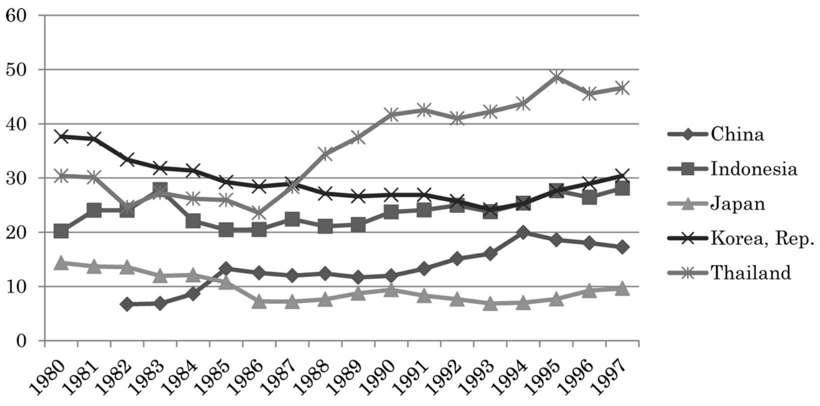
[49] Ades and Di Tella, 1999, p. 985.

[50] Rock and Bonnett, 2004, p. 1013. Note that Rock and Bonnett include Japan in this category even though it cannot be considered "newly industrializing" by this time because of the importance of the Japanese development model to the other members of the group and because of perceived "similarities in domestic political economies of corruption."

high-growth, high-corruption regional peers, Indonesia performs as a slightly above-average player, briefly surpassing South Korea in 1994 to take second place before falling behind again the next year. In sum, placed in full context, Indonesia's economic liberalization during this period can be considered significant in comparison to global and regional averages and above average even among other East Asian developmental states with large domestic markets and comparable political economies of corruption.

Although, by the above standards, Indonesia made great strides in economic liberalization during the 1980s and 1990s, corruption in the 1990s remained widespread. As shown in Table 1 below, Transparency International ranked Indonesia as the most corrupt of the 41 countries evaluated in its CPI survey for 1995. In the CC survey for 1996, the World Bank ranked Indonesia in the 30th percentile on a scale in which 0 represents the most corrupt and 100 the least corrupt. Although Indonesia failed to take the CPI's top spot in 1996 and 1997, it remained in the top quintile of countries surveyed. Table 2 shows the CC percentile ranking and CPI score (which runs from 0 (most corrupt) to 10 (least corrupt)) of Indonesia and the other large East Asian developmental states for the years in the 1990s immediately before Suharto stepped down from power. According to these measures, Indonesia was either the most corrupt (1995 (CPI), 1996 (CC), 1997 (CPI)) or the second-most corrupt (1996 (CPI)) of this highly corrupt (with the exception of Japan) cohort during the waning years of the New Order regime. If these measures are valid, what happened to Indonesia's "corruption dividend?" Why did above-average economic liberalization efforts fail to generate commensurate improvements in the level

Figure 2 Imports of Goods and Services as a Percentage of GDP, 1980–1997



Source: World Bank (http://data.worldbank.org/indicator (downloaded February 4, 2015))

Table 1 Corruption Indices Ranking, Indonesia, 1995–1997

Index	1995	1996	1997
Transparency International CPI Rank	41/41	45/54	46/52
World Bank CC	NA	30.7	NA

Source: Transparency International, Corruption Perceptions Index (CPI); World Bank Worldwide Governance Indicators-Control of Corruption (CC)
Note: CC number indicates percentile rank among all countries (ranges from 0 (lowest) to 100 (highest)).

Table 2 Corruption Indices Scores/Ranking, Japan & Large East Asian NICs, 1995–1997

Country	1995(CPI)	1996(CPI)	1997(CPI)	1996(CC)
China	2.2	2.4	2.9	43.9
Indonesia	1.9	2.7	2.7	30.7
Japan	6.7	7.1	6.6	84.4
South Korea	4.3	5.0	4.3	64.9
Thailand	2.8	3.3	3.1	50.2

Source: Transparency International, Corruption Perceptions Index (CPI); World Bank World Governance Indicators-Control of Corruption (CC)

Note: CPI scores run from 0 (most corrupt) to 10 (least corrupt). CC number indicates percentile rank among all countries (ranges from 0 (lowest) to 100 (highest)).

of corruption?

Identifying the common forms that this corruption took is particularly useful in assessing the validity of the "liberalization as remedy" hypothesis. The first type of corruption, often labeled "petty corruption," involves low-to-mid-level bureaucrats (agents) extorting bribes from citizens (clients) seeking state services. By all accounts, petty corruption was pervasive in Indonesia in the 1990s.[51] Commonly-cited examples of this type of corruption range from a policeman pulling over a car in order to collect a bribe to a local official demanding "special" fees to register the birth of a baby. According to Gray, this type of corruption has a long history in Indonesia.[52]

The second common type is a form of "grand corruption." This term applies to corruption that involves high-level state office-holders (principals) granting significant economic rights, resources or protection (such as import monopolies, government contracts, tax holidays, favorable court decisions, etc.) to private sector actors (clients) in exchange for financial or other undue compensation. Identified as a cause of significant distortions and uncertainty, grand corruption is viewed as more damaging to economic performance than petty corruption.[53] In Indonesia, one form grand corruption took was private sector actors leveraging personal ties with President Suharto and/or his family members to gain economic advantages or exclusive access to state resources. For example, there are many incidences of private firms controlled by Suharto's children or ethnic Chinese business associates successfully lobbying the president to receive preferential access to state lending, special treatment from state regulators, or guaranteed contracts for national infrastructure projects. The extent of state credit extended to firms linked to the Suharto's family is indicated by the fact that such firms figured prominently among the largest holders of non-performing state loans during this period.[54] Prior to the Asian financial crisis, these "crony" firms, which routinely received special treatment from regulators, were even allowed to evade emergency restrictions on foreign borrowing set by the technocrats. In government procurement, "scarcely a single infrastructure project (in the 1990s) was awarded without the partici-

51 Schwartz, 2000, pp. 135–137; Robertson-Snape, 1999, p. 590.
52 Gray, 1979, p. 85–113.
53 Weder, 1999, p. 96.
54 Schwartz, 2000, p. 75.

pation of one Suharto relative or another."[55] Foreign firms were also not immune to this form of corruption. After liberalization allowed foreign investors increased access to the Indonesian market, many actively recruited allies among Suharto's family in order to gain privileges from the government.[56]

A final type of corruption prominent during this period was a purely private sector phenomenon: various forms of illegal, anti-social practices perpetuated by private firms. The banking sector was particularly prone to this form of corruption. Under conditions of free entry and lax state supervision, the mushrooming number of new banks regularly violated legal restrictions on capital adequacy levels and lending to single creditors in rapacious efforts to gain market share.[57] This widespread breach of both the law and public trust led to massive amounts of speculative, unproductive investment that culminated in a series of spectacular bank failures and, ultimately, the massive level of non-performing bank loans witnessed during the Asian financial crisis.

Did Indonesia's economic liberalization during the previous decade fail to reduce the forms of corruption described above in the 1990s? As noted above, existing measures of corruption have been criticized for failing to provide a reliable basis for comparisons over time at the country level and for containing uncontrolled distortions resulting from common cognitive biases. The following analysis addresses both of these shortcomings by utilizing a new measure of corruption developed by Varieties of Democracy (V-Dem), an international academic project to provide valid and reliable measures of democracy across a number of core dimensions.[58] In the context of this broad endeavor, V-Dem asks country experts to assess the frequency of corruption from 0 (most corrupt) to 4 (least corrupt) in the executive, legislative and judicial branches of government as well as in the government bureaucracy and the media. V-Dem measures are available for all countries coded at present for every year from 1900 to 2012, thereby overcoming the longitudinal deficits of popular corruption indices such as the CPI and CC.

V-Dem also addresses the issue of potential biases in a number of ways. First, country experts (coders) are selected using criteria designed to ease the problems of commonly-cited biases such as the bandwagon and halo effects as well as general bias toward Western or Northern hemisphere perspectives. [59] Second, as a minimum of five coders code each question, V-Dem is able to conduct inter-coder reliability tests to identify rogue coders, a standard practice in political science but one rarely if ever used in existing corruption measures.[60] Finally, employing latent variable models, V-Dem uses inter-coder agreement and disagreement to estimate reliability and systematic bias to make adjustments

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[55] Ibid., pp. 313–319.

[56] Ibid., p. 158; See also the example of the Bre-X gold mine scandal in Robertson-Snape, 1999, p. 596.

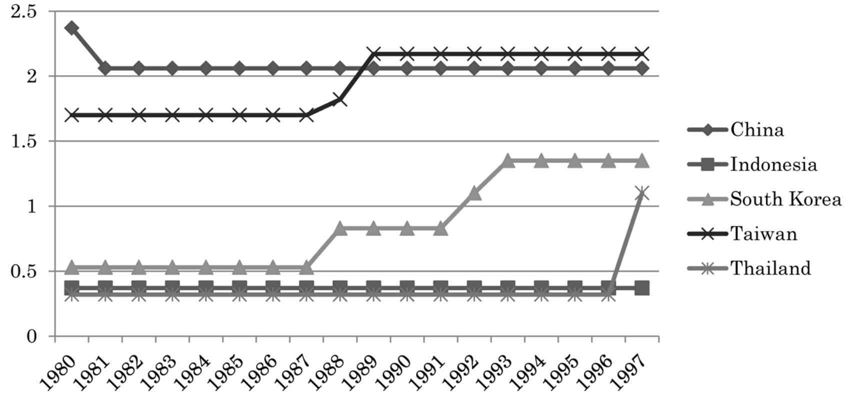
[57] Robison and Rosser, 1998, p. 1599.

[58] See the Varieties of Democracy (V-Dem) website at https://v-dem.net. Note that the first version of the V-Dem database was made available to the public in spring 2014.

[59] Country experts are selected for their expertise (coders have degrees in related fields such as the social sciences, a record of relevant publications, and/or hold positions that indicate relevant expertise (e.g. noted journalist, etc.)), nationality (most coders are citizens or permanent residents of the countries they code), impartiality (coders are vetted to ensure they are not obligated to powerful actors or spokespersons for particular political parties or ideologies), and diversity of background (coders from different professional and institutional backgrounds are assigned to code each country). Coppedge, et al., 2014a, pp. 14–15.

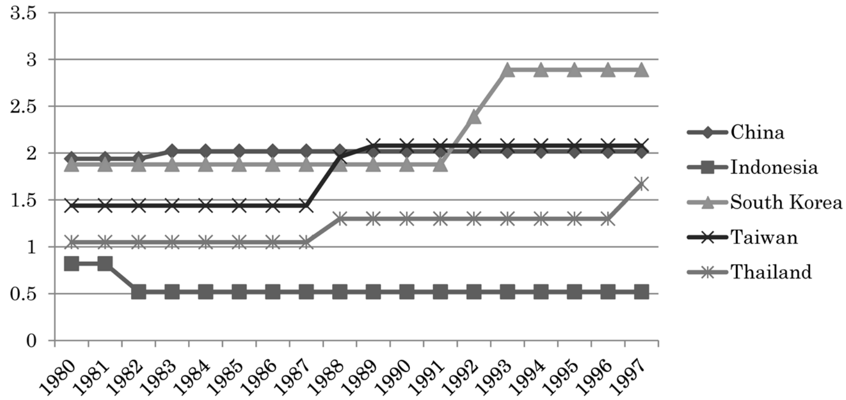
[60] Ibid., p. 16. For more on methods of establishing inter-coder reliability, see Neuendorf, 2002, 99.141–166.

Figure 3 Executive Bribery and Corrupt Exchange, 1980–1997



Source: V-Dem (https://v-dem.net (downloaded February 2, 2015))
Note: V-Dem scores here run from 0 (most corrupt) to 4 (least corrupt).

Figure 4 Executive Embezzlement and Theft, 1980–1997



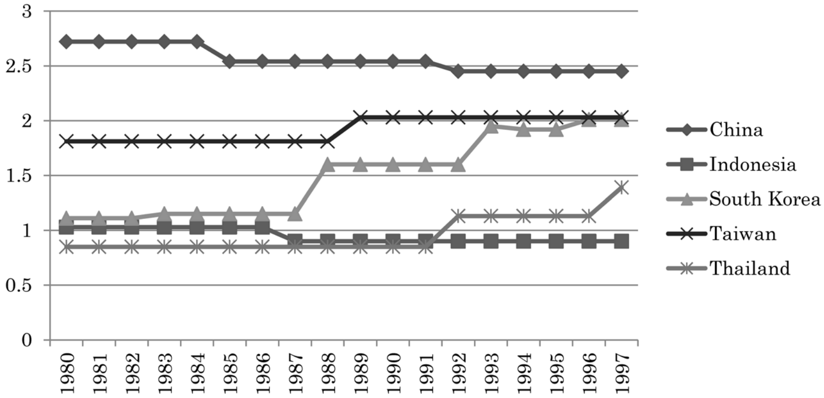
Source: V-Dem (https://v-dem.net (downloaded February 2, 2015))

in order to combine coder ratings into a "best estimate" result for each question.[61] In sum, V-Dem offers a measure of corruption that is unparalleled in terms of the range of actor types individually evaluated, the length of time for which annual comparisons can be made at both the country and cross-country levels, and the amount of attention given to detecting and correcting for well-known sources of bias.

V-Dem offers two separate measures of executive branch corruption, asking country experts to assess how often members of the executive branch or agents acting on their behalf "grant favors in exchange for bribes, kickbacks, or other material inducements" and "steal, embezzle, or misappropriate public funds or other state resources for personal or family use."[62] V-Dem results for 1980–1997 appear

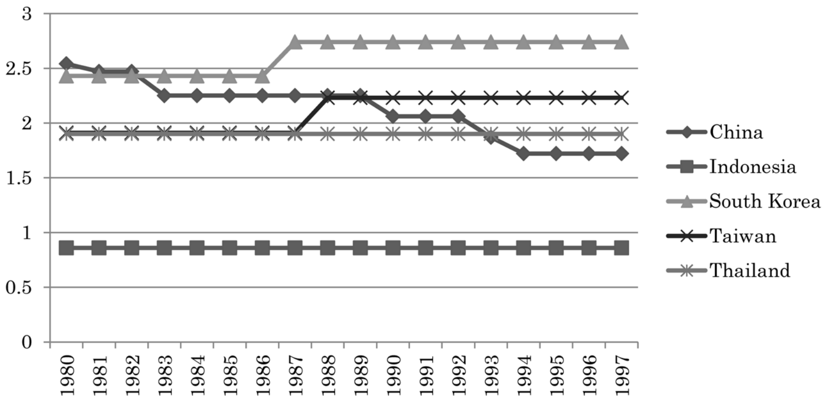
[61] Coppedge, et al., 2014a, pp. 16.
[62] Coppedge, et al., 2014b, pp. 166–167.

Figure 5 Legislature Corrupt Activities, 1980–1997



Source: V-Dem (https://v-dem.net (downloaded February 2, 2015))

Figure 6 Judicial Corruption in Decisions, 1980–1997

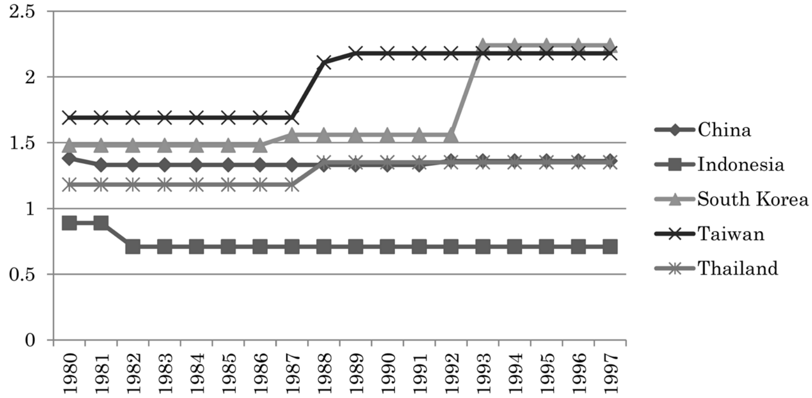


Source: V-Dem (https://v-dem.net (downloaded February 2, 2015))

in Figures 3 and 4. To maintain a measure of cross-country comparison, Indonesia's results are shown together with results for the other large East Asian developmental states, with Taiwan substituted for Japan, one of the countries for which V-Dem results are not available as of this writing.[63] Figures 3 and 4 reveal an executive branch that maintained a relatively high level of corrupt exchanges while actually increasing the extent of its theft of state resources as economic liberalization reforms commenced. In addition, the level of executive corruption in Indonesia exceeds that of the other large East Asian developmental states, with the exception of Thailand on the bribery measure. In particular, the frequency at which state resources are thought to be embezzled by the Indonesian executive branch seems distinct among this sample of developmental states.

[63] Rock and Bonnett do not include Taiwan in their analysis even though it is prominently featured in the literature on developmental states in Asia, has a comparable political economy of corruption, and has a population that exceeded 20 million (Rock and Bonnett's cut-off line between small and large countries) in the late 1980s. Rock and Bonnett, 2004, p. 1011.

Figure 7 Public Sector Corrupt Exchanges, 1980–1997



Source: V-Dem (https://v-dem.net (downloaded February 2, 2015))

Principals involved in corruption can also be found in the legislative and judicial branches of government. Figures 5 and 6 show the V-Dem results for these branches.[64] The results for the legislature show a body that while on par with the executive branch in bribe-taking (if not embezzlement) actually grew slightly more corrupt after many of the economic liberalization reforms were in place. On the other hand, the judiciary apparently maintained an unchanging but extremely high level of corruption in their decisions. Among government actors, the judiciary is rated the second most corrupt next to the executive with regard to bribery and is rated the most corrupt bench among those of the developmental states here.

V-Dem also provides a measure of the agent most commonly modeled in the corruption literature by asking how often public sector employees take bribes for administrative favors.[65] As with executive embezzlement, corruption in the bureaucracy worsens just prior to the onset of major economic liberalization reforms in 1983 and then remains unchanged at a comparatively high level for the remainder of the New Order regime.[66]

Although V-Dem does not ask about client corruption in the private sector generally, it does include a question about corruption in one specific industry, the media.[67] During Suharto's rule, this industry was heavily-regulated (with ownership strictly controlled by the Ministry of Information), included a state-owned member (Televisi Republik Indonesia (TVRI)), and was largely staffed by journalists known to practice self-censorship for fear of government-imposed bans. However, scholars have identified the media as one of the growing and lucrative sectors of the Indonesian economy during the eco-

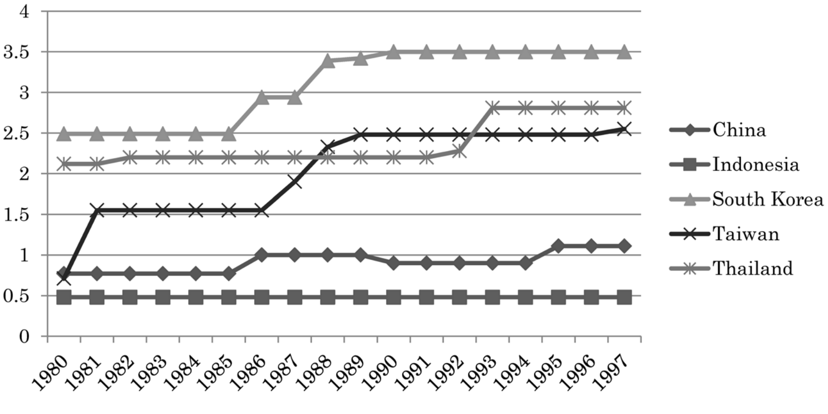
64 The legislature question asks: "Do members of the legislature abuse their position for financial gain?" Coppedge, et al., 2014b, p. 179. The judiciary question asks: "How often do individuals or businesses make undocumented extra payments or bribes in order to speed up or delay the process or to obtain a favorable judicial decision?" Coppedge, et al., 2014b, p. 205.

65 The public sector employee question asks: "How routinely do public sector employees grant favors in exchange for bribes, kickbacks or other material inducements?" Coppedge, et al., 2014b, p. 167.

66 Pincus and Ramli date the beginning of banking reforms from this year, see Pincus and Ramli, 1998, p. 725.

67 The media question asks: "Do journalists, publishers, or broadcasters accept payments in exchange for altering news coverage?" Coppedge, et al., 2014b, p. 278.

Figure 8 Media Corruption, 1980–1997



Source: V-Dem (https://v-dem.net (downloaded February 2, 2015))

nomic liberalization period. As Frederick and Worden note, "The trend toward somewhat greater pluralism and openness had begun in the late New Order, when the regime allowed the founding of a number of new television and radio stations."[68] In particular, large viewing audiences made these new television ventures very profitable. Although licenses were only granted to "various Suharto family members, cronies, and other wealthy conglomerates," the increasing competition among stations for advertising revenues encouraged broadcasters to push the boundaries of regime censorship to draw in viewers.[69] Further, locked in a web of regime ties and high rents, the new stations could not be easily disciplined by the Suharto government when they crossed lines in their reporting. As Brown concludes: "The interlocks between banking, business, politics, military, and [Suharto] and his family were intense, high and located within monopolies in cement, oil timber, telecommunications, media and food where rents were high."[70] Despite the media's more publically-minded role in other polities and the Suharto government's past record of media suppression, it is argued here that the media provides a relatively representative example of a growing and powerful private sector industry during the economic liberalization period. In this regard, the results of V-Dem's question about media corruption can be said to shed at least some light on expert views about the wider state of corruption among private sector firms.

The V-Dem results paint a bleak picture of a highly corrupt media even by the standards of large developmental states in the region. In addition, the frequency of corruption remains static through the last decade and a half of the New Order regime, indicating in the very least a remarkable resistance to the pressures to reduce corruption supposedly created by economic liberalization reforms.

Why did economic liberalization in Indonesia during this period fail to yield reductions in the forms of petty and grand corruption described earlier? Table 3 reveals an important finding. It shows

[68] Frederick and Worden, 2011, p. 287.
[69] Ibid.
[70] Brown, 2006, p. 958.

Table 3 Corruption Averages, Principals, Agents and Clients in Indonesia, 1983–1997

Actor	Average
Principal: Executive Corruption Average (Bribery + Embezzlement / 2)	0.45
Client: Media Corruption	0.48
Agent: Public Sector Corrupt Exchanges	0.71
Principal: Judicial Corruption	0.86
Principal: Legislature Corrupt Activities	0.93

Source: V-Dem (https://v-dem.net (downloaded February 2, 2015)); Averages calculated by author.
Note: Executive Corruption Average is the average over the fifteen-year period of the two indicators of exectutive corruption: executive bribery and corrupt exchanges and executive embezzlement and theft.

the average corruption scores over the fifteen-year period of economic liberalization under Suharto for each of the individual actors. The actors rated the most corrupt over this period turn out not to be the agent (government bureaucrats) whose corrupt behavior is thought to be modified by liberalization in the "liberalization as remedy" hypothesis, but rather the main principal involved and the only client included in the evaluation. This indicates a need to reconsider the relationship between economic liberalization and corruption in a number of ways.

First, the Indonesian case reveals an important theoretical flaw in the "liberalization as remedy" hypothesis: its overemphasis on agent-to-client forms of corruption. Advocates of this hypothesis largely overlook the significance of corruption in which the principals and/or the client are the corrupt actors.[71] By focusing exclusively on the behavior of agents (i.e. government bureaucrats), the "liberalization as remedy" hypothesis assumes the benevolence of both principals and clients. In this way, it fails even to consider, let alone provide a remedy for, the two most highly-rated forms of corruption in the Indonesian case.

This oversight creates problems for the validity of the hypothesis on multiple grounds. First, by positing benevolent principals and clients, the "liberalization as remedy" hypothesis is grounded in assumptions that do not hold in many real world cases and are particularly problematic in authoritarian regimes. Although, as will be further discussed in the final section, political liberalization does not always lead to the institutionalization of adequate checks on the rent-seeking of corrupt principals and clients, the impact of economic liberalization implemented under an authoritarian regime is particularly sensitive to the corruption of these actors. By not contemplating what corrupt principals and clients can mean for economic liberalization in an authoritarian setting, the "liberalization as remedy" hypothesis fails to account for variables central to understanding the outcomes of such reforms in an important subset of cases.

Second, by underplaying principal and client corruption, the theory fails to consider sufficiently the possibility that these forms of corruption can distort the economic liberalization process itself. The

[71] Examples of this startling omission include Klitgaard, p. *x*, 1988; Ades and Di Tella, 1999, p. 988. For discussion of the implications of a corrupt principal for understandings of corruption, see Lambsdorff, 2002.

perversion of this process through grand corruption appears to have been a common occurrence in Indonesia.[72] For example, although some trade reforms, such as the privatization of customs functions, did succeed in reducing some petty corruption (agent-to-client), other deregulation measures were rendered meaningless by principal/client corruption. A prominent example is the IMF-mandated abolishment of the plywood cartel in 1998. Although control of the sector was officially removed from Apkindo (Indonesian Wood Panel Association), Apkindo chief and Suharto associate Bob Hasan succeeded in maintaining a stranglehold on the industry by forcing all firms to use his shipping service.[73]

A third weakness attributable to the myopic focus on agent-based forms of corruption involves the new opportunities for corruption created when liberalization is implemented in the face of unchecked principal and client corruption. For example, although privatization programs were intended to reduce corruption by limiting bureaucratic power in the economy, collusion among Suharto and private firms associated with his family warped these efforts into "little more than a transfer of assets to Indonesia's political elite, with only a modest increase in competition."[74] This was particularly true in the telecommunications sector, where the sale of new licenses to private firms left the entire cellular telephone market in the hands of the Suharto family and their business partners.[75] As noted earlier, this was also true in the media industry, where a loosening of strict government control over market entry resulted in the first three licenses granted for private television stations in Indonesia going to one of Suharto's sons (RCTI in 1989), one of his cousins (SCTV in 1990), and one of his daughters (TPI in 1991).[76] In sum, liberalization's failure to provide a remedy for corruption in Indonesia can largely be attributed to its difficulty in addressing non-agent forms of corruption. Indeed, far from dismantling all of the corrupt networks that linked principal and client, there is strong evidence that liberalization programs actually created new opportunities to profit from these illicit ties.[77]

Another reason why liberalization failed to remedy corruption in Indonesia in the 1990s involves the difficulties of changing the role of the developmental state in the economy. In implementing liberalization measures, the technocrats weakened the "reciprocal control mechanism" of the developmental state without creating a new regulatory regime to oversee newly liberalized sectors. In the reciprocal control mechanism, the developmental state allocates intermediate assets to make manufacturing profitable but holds recipients to monitorable performance standards that are both re-distributive and results-oriented.[78] Economic liberalization weakens this mechanism by reducing the state's direct role in disciplining market actors. If the state fails to replace this control mechanism with an effective regulatory capacity, liberalization can lead to a "regulatory vacuum" in which private sector actors are left largely without state oversight in newly deregulated markets, a situation that virtually assures an increase in

72 For examples, see Rosser, 2002; Rock, 2003; and Brown, 2006.
73 Robison and Rosser, 1998, p. 1602.
74 Schwartz, 2000, pp. 314–315.
75 Ibid., p. 315.
76 Nugroho, et al., 2012, p. 37.
77 Pincus and Ramli, 1998, p. 732.
78 Amsden, 2000, p. 10.

private sector corruption. In the Indonesian case, the technocrats' failure to expand the bureaucracy's capacity to oversee deregulated industries was directly responsible for creating new opportunities for corruption in the private sector. This was nowhere more prevalent than in the banking sector. The routine violation of capital adequacy requirements and lending limits by newly established banks pursuing speculative investments was greatly facilitated by lax state oversight. As Schwartz concludes, "by not installing adequate safeguards against fraudulent and imprudent lending, the technocrats exposed the banking system to dangers that would come back to haunt Indonesia in the late 1990s."[79]

Finally, according to the V-Dem results reported in Figure 7 above, economic liberalization in Indonesia during the 1980s does not seem to have had much impact on the agent-related corruption such reforms are supposed to address. Rosser suggests one possible explanation: The trajectory of economic liberalization was from the start fundamentally shaped by the interests of government bureaucrats, particularly in the trade and investment spheres.[80] Having gained a number of rent-generating opportunities through past state interventionist policies, including the management of monopolies granted to various state-owned enterprises, administrative controls in trade and investment policy, and control of state financing for high-technology industries, government bureaucrats strongly resisted liberalizing reforms that reduced their ability to access these rents. Although they were forced in some cases, such as in the reform of the customs system, to surrender treasured functions that provided considerable opportunities for agent rent-seeking, government bureaucrats were able to use their power in the New Order regime to redirect liberalization efforts away from their most-cherished administrative prerogatives. From the client side, the large business conglomerates also wielded their considerable influence to protect their own rent-generating schemes built out of developmental state policies. As a result, even at the onset of the Asian financial crisis, "many of the politico-bureaucrats' and the conglomerates' most lucrative monopolies, cartels, and other trade and investment arrangements were still in place and several new ones had been introduced."[81] This indicates considerable room for the resistance of powerful agents and clients to sustain rent-generating institutions and corrupt practices even in the face of far-reaching economic liberalization reforms.

Can the "liberalization as remedy" hypothesis be repaired? This section concludes by introducing an informal model that attempts to resolve some of the problems highlighted above. First, the model begins with the assumption that principals and clients are corrupt, the regime is an authoritarian developmental state, and the country has a large population (in excess of 20 million). Second, as key players in the old developmental state, bureaucratic agents are assumed to be relatively benevolent (in the weak sense of more frequently prioritizing key development goals over individual or organizational gain) at the start of the liberalization process but increasingly incapable of limiting corruption and likely more complicit in it as the process proceeds. Finally, Kang's model is adapted to address the

[79] Schwartz, 2000, p. 317.
[80] Rosser, 2002.
[81] Rosser, 2002, p. 124.

Table 4 The Effect of Economic Liberalization on Corruption in Authoritarian Developmental States

	Corrupt Principal in Coherent Authoritarian State	**Corrupt Principal in Incoherent Authoritarian State**
Corrupt Clients in Concentrated Business Sector	I. Mutual Hostages Result: Corruption remains the same Example: Indonesia in the 1990s	II. State-Looting Result: Corruption increases Example: Philippines under Marcos
Corrupt Clients in Dispersed Business Sector	III. Predatory State Result: Corruption increases Example: China after 1978	IV. Open Door Result: Corruption decreases Example: Thailand in the 1990s

question of whether economic liberalization is likely to reduce corruption in this specific developmental setting.[82] Table 4 below summarizes the adapted model.

The model posits four potential power structures depending on the level of state coherence and the level of concentration in the business sector. In the first quadrant, economic liberalization is conducted by cooperating but corrupt principals and clients who had achieved a rough balance of power under a coherent authoritarian developmental state and now variously collude and compete for rents generated from the design of new liberalized economic institutions. Although some rent-seeking arrangements established under the developmental state will have to be abandoned during the liberalization process, new opportunities for rent-seeking will also be developed and exploited. The end result will likely be little change in the overall level of corruption. This scenario best fits the case of Indonesia in the 1990s.

Power imbalances between the public and private sectors yield two different but arguably equally poor outcomes. In the second quadrant, corrupt clients are the driving force behind economic liberalization in an incoherent authoritarian regime led by corrupt principals. Here, reforms will privilege these corrupt private sector actors, ensuring the protection of monopolies and other rent-generating opportunities they gained under previous developmental state policies while constructing new ones through selective deregulation and the looting of state resources. The overall result will be an increase in the level of corruption. The Philippines under the Marcos dictatorship is an illustrative example of cases in this quadrant.[83] In the third quadrant, corrupt principals introduce economic liberalization in an authoritarian regime with high state coherence and a private sector of dispersed corrupt clients. Reforms that deregulate and open the economy are thus inevitably also designed in part to redirect rents

82 Kang, 2002, p. 182.

83 Hutchcroft argues that the Philippines both during and shortly after this period is a case of “booty capitalism” in which “a powerful oligarchic business class [clients] extract privilege [rents] from a largely incoherent bureaucracy [agents],” while high government officials such as Marcos (principal) collude with the corrupt clients to steal vast sums from state financial institutions. See Hutchcroft, 1998, p. 20.

from weaker clients to the principals and possibly also their client allies and to preserve the principals' existing rent-generating networks established under the old developmental state. The overall result is again an increase in corruption in comparison with the period before economic liberalization began. China after the economic liberalization reforms began in 1978 is as an example of this category.[84]

Finally, the fourth quadrant is populated by incoherent states led by corrupt principals who face dispersed private sectors of corrupt clients in a political economy with many veto players. The model in this quadrant rests on three assumptions: 1) To the extent a meaningful program of economic liberalization can be implemented in these circumstances, it will be driven in part by powerful foreign investors and lenders; 2) Due to state incoherence and the weakness of the business class, foreign investors and lenders will have more capacity to demand corruption be controlled than they do in other quadrants; and 3) Principals, agents and clients will seek alliances with each other to extract rents from the new liberalized institutions, but competition among these actors will reduce total returns on rents. The overall result is predicted to be a decrease in the level of corruption. Thailand in the 1990s can arguably be said to fit into this category.[85] In sum, the amended model predicts four possible trajectories for the pattern and level of corruption in a liberalizing authoritarian developmental state, only one of which involves corruption declining.

IV. Conclusion

The unmistakable lesson of the Indonesian case for other developmental states is that economic liberalization conducted under continued authoritarian rule does not necessarily reduce corruption. As the model developed above shows, in the majority of scenarios involving authoritarian developmental states, corruption either increases or remains the same with the introduction of economic liberalization. More specifically, although liberalization may reduce agent corruption in some instances by taking away the discretionary powers bureaucrats use to extract bribes, it may have limited effects on agent behavior and no ameliorative impact on principal and client forms of corruption. Further, in the context of the developmental state, shifting the control mechanism from the state to the market is a

[84] See Guo, 2008, pp. 354–364; Lu, 2000, pp. 288–292, and the discussion of these works in the concluding section.

[85] Although known for having a greater bureaucratic capacity (effective, benevolent agents) than the Philippines and having already undergone a degree of political liberalization, Thailand in the 1990s fits this category for the following reasons. First, although not a "hard" authoritarian state during this decade, Thailand was at best a "semi-democracy" and was rated "free" by Freedom House for only three years of the decade (1990, 1998, and 1999). See Freedom House website at: https://www.freedomhouse.org (downloaded February 2, 2015). Second, until the early 2000s, Thailand was more dependent on Official Development Assistance (ODA) than the world average (measured as US$/per capita) and far more dependent than the East Asia and Pacific regional average. See World Bank website at: http://data.worldbank.org/indicator (downloaded February 6, 2015). In addition, Foreign Direct Investment (FDI) into Thailand increased dramatically after the 1985 Plaza Accord caused currency appreciation in Japan and other East Asian NICs, rising from around US$1 billion in 1986 to US$5.1 billion in 1998. Puapan, 2014, pp. 4–5. Third, although Rock notes that a relatively strong bureaucracy played a key part in Thailand's effort to realize a "Northeast Asian style developmental state," by the late 1980s and early 1990s, the core bureaucracies of macroeconomic governance had been politicized by the influx of corrupt principals (initially provincial politicians). The decline of these bureaucratic institutions left Thailand in the grip of a "decentralized corruption free for all." Rock, 2009, p. 941. Finally, MacIntyre argues that Thailand during this period had a surfeit of veto players, thus making policy change difficult. MacIntyre, 2001, p. 94.

process fraught with peril for reformers seeking to limit corruption. When confronted with pervasive principal/client corruption combined with weak regulatory capacities among bureaucrats, economic liberalization fails to provide clear mechanisms for reducing total corruption and may actually present new opportunities for corruption in some sectors. In addition, since institutions associated with controlling principal/client corruption, such as competitive elections, a free media, and independent judiciary/law enforcement, have been consistently weak in Indonesia as in other authoritarian developmental states, liberalization does not seem a particularly promising anti-corruption policy for these countries. As Pincus and Ramli aptly conclude: "If we have learned anything from the Indonesian crisis it is that where governments fail, markets are bound to fail as well sooner or later. The idea that economic liberalization is a substitute for a fair and effective state is a dangerous fallacy, and one that Indonesia's new leaders should resist at all costs."[86]

A single case study, no matter how instructive, is not sufficient to infirm a hypothesis as general as "liberalization as remedy." However, the conclusions here are reinforced by the findings of research on economic liberalization and corruption in other authoritarian developmental states.[87] In particular, case studies of China have found that the economic liberalization begun there in 1978 has led to increased corruption.[88] For example, in a study of principal/agent corruption, Guo finds that discovered cases of corruption increase in scale (i.e. size of bribes, etc.) and number in both categories of grand and petty corruption from 1978 through the mid-1990s.[89] In addition, Guo notes a number of specific linkages between the discovered cases and economic liberalization reforms, concluding "[a]lthough not all corruption cases are the results of the economic transition, nearly all cases are influenced by it."[90] Wedeman, while also noting an initial quantitative increase in all forms of corruption, argues a qualitative shift occurred in the 1990s, which saw an increase in cases of grand corruption involving senior officials that were usually linked to economic offences.[91] By contrast, Lu focuses on the proliferation of corruption by agents working for Chinese government organizations and argues China has developed a system of "booty socialism" that contrasts with the "booty capitalism" of the Philippines in that private sector agents are unable to resist state predation, and corrupt agents (bureaucrats), rather than corrupt principals and clients, are most responsible for the advance of the predatory state in post-reform China.[92]

If economic liberalizatinon is unlikely to reduce corruption when employed by large authoritarian developmental states, what can these states do to control corruption? Unfortunately, existing research

86 Pincus and Ramli, 1998, p. 733.

87 In addition to examples previously-cited with regard to the Philippines, China and Thailand, see James, 2010 (Thailand and Myanmar); Case, 2008 (Malaysia); Holmes, 2008 (Russia); and Dininio and Orttung, 2005 (Russia).

88 In addition to the works discussed below, see Sun and Johnston, 2009.

89 Further, as the "average latency period" – the period between when a corrupt act is committed and when it is discovered – has continued to increase over time, Guo argues evaluating the state of corruption after the mid-1990s using discovered cases may underestimate corruption. Guo, 2008, p. 354–364.

90 Ibid., p. 364.

91 Wedeman, 2004.

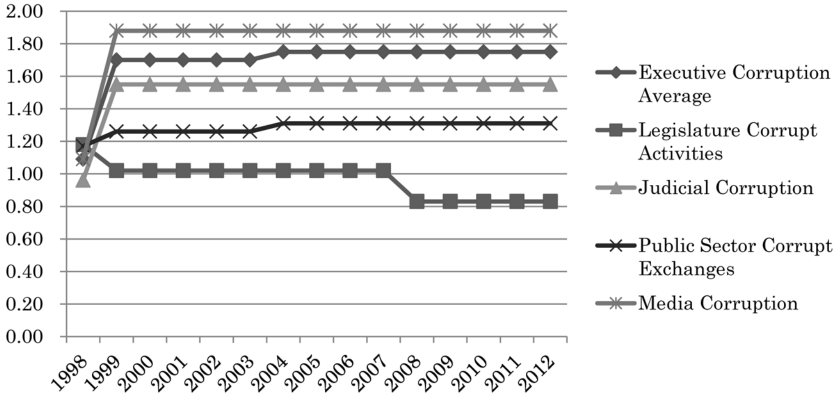
92 Lu, 2000, pp. 288–292.

fails to offer clear answers to this important question. Although political liberalization and democratization are widely regarded as the ultimate means of controlling corruption, especially by principals, recent research has cast doubt on this assertion. As noted earlier, Kang argues that democratization reoriented South Korea's developmental state by reducing state coherence through increased competition for elective office among political leaders. At the same time, Korean business groups remained concentrated and corrupt and were better able to influence the state through political campaign donations, especially under the conditions of weak legal institutions. The result was a shift from the "mutual hostages" collusion between government principals and corporate clients that limited corruption to some extent under authoritarian rule to a new world of nearly unchecked business rent-seeking and an overall increase in the level of corruption.[93] Sun and Johnston, in comparing corruption in democratic India and authoritarian China, also find that political liberalization in India failed to control corruption any better than efforts in China. They conclude: "Economic liberalization and democratization seem to encourage the opening up not only of official processes, but also of corrupt ones."[94] In addition, as the experience of Latin America has shown, the implementation of simultaneous political and economic liberalization can actually foster more corruption.[95] Political liberalization should thus not be seen as a panacea for cleaning up corruption left over from the authoritarian pasts of developmental states.

One hopeful finding drawn from quantiative studies on the causes of corruption is that the relationship between political liberalizaton and corruption may be nonlinear. In particular, Montinola and Jackman find that corruption "is typically a little higher in countries with intermediate levels of political competition than in their less democratic counterparts, but once past the threshold, higher levels of competition are associated with considerably less corruption."[96] This means that countries that partially democratize generally have more corruption than their authoritarian colleagues but as democratization deepens and political competition expands, countries suffer far less amounts of corruption.[97] Since the establishment of effective norms and institutions to foster political competition often take new democracies time to develop and diffuse, this suggests countries that persevere or "muddle through" heightened levels of corruption during the first years of democratization can expect to see improvement once they develop the capacity to host more political competition. This dovetails with Treisman's finding that long exposure to democracy is associated with lower levels of perceived corruption. Although statistically significant, the effect is small, in essence demanding decades of exposure to democracy to make large dints in the level of a country's perceived corruption.[98] It appears the democratic route to a less-corrupt society is a marathon, not a sprint.

[93] Kang, 2002, pp. 193–200.
[94] Sun and Johnston, 2009, p. 15.
[95] Weyland, 1998.
[96] Montinola and Jackman, 2002, p. 167.
[97] Ibid.
[98] Treisman, 2000, p. 433.

Figure 9 Corruption in Indonesia, 1998–2012



Source: V-Dem (https://v-dem.net (downloaded February 2, 2015)); Averages calculated by author.

What do these findings mean for Indonesia moving forward? As the country deepens its experience with democracy, will it experience a lower frequency of corruption? Figure 9 summarizes the V-Dem results for all actor types evaluated for corruption in Indonesia for the period after Suharto stepped down in 1998 through 2012.

These results reveal both hopeful and troubling trends. First, the two actors rated the most corrupt on average during the period of economic liberalization under the New Order regime, the executive branch and media, were judged the least corrupt among the actors evaluated in the subsequent period. The ratings for corruption in the judiciary and bureaucracy also improved following democratization, although not by the same degree. In fact, even the actor viewed as the most corrupt in the new Indonesian democracy, the legislature, actually improved its average rating slightly between 1983–1997 (0.93) and 1998–2012 (0.97). What is troubling here is that, nearly a decade and a half since the end of Suharto's reign, experts still rate most of Indonesia's key institutional actors as fairly corrupt, including the judiciary and media, which are viewed as vital checks on executive and legislative power and corruption. In addition, the fact that the legislature, which is perhaps the most-newly empowered among the actors, saw its rating actually fall over the democratic era points to the possibility of new avenues of corruption being opened.

In 2014, Freedom House lowered Indonesia's rating in civil liberties and moved the country's status from free to partly free. Although the rating change was linked to the passage of a law restricting the activities of non-governmental organizations and requiring them to support the national ideology of Pancasila, which includes a religious component, Freedom House's review of Indonesia in 2014 is also replete with references to corruption, including "corruption remains endemic," "plagued by corruption," "rife with corruption" and the sobering conclusion that "the ability to obtain private business licenses and public employment is often limited by the need for bribes or other inducements…[c]orruption also affects businesses' daily operations and routine interactions with the state bureaucracy."[99] Although this assessment may represent only a brief setback for Indonesian democracy, only time will tell. On the whole, the picture of contemporary Indonesia developed here can at least be said to depict a relatively young democracy in the process of muddling through…hopefully on its way to finding a less corrupt future.

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